Moreover, the Commission must abandon the flawed notion that rates must be "affordable." "Affordability" is completely subjective in nature. What the Commission must understand is that the "just and reasonable" standard only requires that prices fall within a "zone of reasonableness" – *i.e.,* that these rates are neither "excessive" (rates that permit the firm to recover monopoly rents) nor "confiscatory" (rates that do not permit the regulated firm to recover its costs). They need not – just like caviar or Rolls Royce limousines – be "*fair*" or "*affordable*" for everyone.[34]

Similarly, the Commission is going to have to determine whether the firm(s) under its jurisdiction are single-output or, more likely in today's era of "convergence," multi-product firms. As such, whenever the Commission attempts to define a firm's rate (*i.e.*, define the zone of "zone of reasonableness"), a primary focus on a multi-product firm's *aggregate* profits is irrelevant. Rather, the appropriate scope of the Commission's inquiry must be whether the specific profits derived from providing *regulated* products and services (and *not* from ancillary businesses or investments) are the result of the regulated company's ability to charge an excessive (*i.e.,* monopoly) rate for the regulated product or service – *i.e.,* the product or service over which it can raise price or strict output absent regulation. If the rate reflects the regulated company's true costs of

---

[34] *See Farmers Union Central Exchange, Inc. v. FERC,* 734 F.2d 1486, 1504 (D.C. Cir.), *cert. denied sub nom.*, 469 U.S. 1034 (1984) (the concept of "just and reasonable" must clearly be more than a "mere vessel into which meaning must be poured."); *but c.f., Southwestern Bell Telephone*, 1998 WL 485387 (8th Cir. Aug. 19, 1998) ("Access charges imposed on IXCs that include the LECs' universal service cost are not "above cost" *since universal service contributions are a real cost of doing business.*") (Emphasis supplied.) TEC is interested to find out, however, exactly which hornbook or what theorist the court is referring to that recognizes the concept of "real" as a legitimate type of economic cost.

providing the regulated product or service, but the Commission nonetheless believes that this J&R rate is "too expensive," "unfair," or not sufficiently "affordable," then it is therefore wholly improper for the FCC to require the regulated firm to "subsidize" the price it charges for its regulated service with ancillary profits just to make the rate more politically "affordable" or "fair." When this occurs, "affordable" simply becomes an excuse for the Commission to set unlawfully confiscatory rates instead.[35]

Another consequence of multi-product offerings is that cost-allocations decisions will be increasingly important if the Commission decides to engage in price regulation. For instance, recent attempts by ILECs to allocate *all* local loop costs to its monopoly voice service customers and away from its competitive xDSL services – despite the fact that the same loop facility support both services—must be examined carefully and resolved if the FCC believes that rate regulation has a place in this environment.[36] Otherwise, the exercise of reviewing these ILEC tariffs will be a worthless and counter-productive exercise, because approval of these bogus tariffs would confer a modicum of regulatory approval of this practice.

---

[35] *See, e.g.*, Christopher Stern, *FCC Chief Eyes Cable Rate Cap*, Reuters (Jan. 14, 1998) (Reporting that Kennard is "pondering" limits on amount of programming costs cable companies may pass on to consumers. Kennard questioned whether it was "right" to permit cable companies to pass on all programming costs to consumers, adding "Should the consumer shoulder all the increased costs of programming?" As a possible mitigation measure, Kennard suggested that increased programming expenses should be offset for consumers through other revenues including advertising, commissions, and payments by programmers for carriage.)

[36] *See, e.g.*, GTE Telephone, GTOC Tariff No. 1, GTOC Transmittal No. 1148,CC Docket No. 98-79.

Accordingly, because regulation is supposed to be the substitute for, and not the complement of, competitive rivalry, the Commission should attempt to set a rate that approximates the equilibrium price (*i.e.,* where supply equals demand) that a rivalrous market would produce, including a rational allocation of fixed and shared costs. But if the Commission truly wants to make prices for a "public" good or service more "affordable" – regardless of whether the end-price for this product or service is set by regulation or not – then the Commission needs to focus its priorities on promoting entry and rivalry, such that firms will be forced to innovate and lower costs and, with such innovation and increased efficiency, force supply and demand to move down and to the right. If this shift occurs, then the entire "zone" should therefore also be forced down and to the right over time. So long as the Commission maintains a static, "incumbent-centric" approach, however (*i.e.*, the incumbent is the only source of distribution), it will provide firms with no real incentive to innovate and lower costs and, as such, true de-regulation and competition will never occur.

2. *Conduct Regulation*

Conduct regulation is usually used to mitigate various types of strategic, anticompetitive behavior, such as undue discrimination to bottleneck facilities, input foreclosure, raising rivals' costs, *etc.* Again, because market structures are not homogeneous, conduct regulation also can take many forms. For example, there may be "passive" types of conduct regulation, where the Commission may impose special reporting requirements on one specific class of firms (*e.g.,* "dominant" firms). Similarly, the Commission may permit the rates of "non-dominant" firms to go into effect immediately, but require any new tariffs from "dominant firms" to endure prolonged notice and comment periods before the rates may go into effect. Conduct regulation may take more "active" forms as well. For example, a firm may have to demonstrate that the economic costs resulting from an exclusive distribution contract do not outweigh the efficiency benefits created by this exclusion.[37] Similarly, a firm might be obligated to provide rivals non-discriminatory access to its network based on a particular cost methodology.

Under any scenario, however, the concept of conduct regulation always implies that the Commission will take enforcement action against one or more firms only when it comes to the FCC's attention – either by complaint or *sua sponte* – that the regulated firm has acted contrary to the Commission's rules. In other words, enforcement of alleged acts of anticompetitive conduct will essentially occur on a case-by-case basis and, moreover, the responsibility for effective enforcement lies squarely on the Commission's shoulders. The big problem, however, is that the FCC has a very poor track record for effective and judicious enforcement against one or more firms' ability to exercise market power.[38] Thus, as Judge Frank Easterbrook wrote over ten years ago, the "principle that

---

[37] For a detailed exegesis of the FCC's program access rules, *see* James W. Olson & Lawrence J. Spiwak, *Can Short-Term Limits on Strategic Vertical Restraints Improve Long-Term Cable Industry Market Performance?* 13 CARDOZO ARTS & ENT. L. J. 283 (1995).

[38] *See* Thomas W. Hazlett and George S. Ford, *The Fallacy of Regulatory Symmetry: an Economic Analysis of the "Level Playing Field" in Cable TV Franchising Statutes* (1997) (unpublished manuscript) (notion of "fair, competition-like outcomes" is ridiculous because regulators will never "choose 'efficient' prices, outputs, and quality costlessly and with perfect information."); Harold Demsetz, *Information and Efficiency: Another Viewpoint,* J.L. & ECON. (Apr. 1969) at 1-22; Paul McNulty, *Economic Theory and the Meaning of Competition*, 82 Q.J. ECON. 639-656 (1968)).

regulation must extend to catch all substitutions at the margin has a corollary: *if you're not prepared to regulate thoroughly, don't start.*"[39]

The FCC has, laudably, recently attempted to restructure its common carrier enforcement procedures.[40] However, there still seems to be a lack of will or confidence at the FCC to take its powers seriously and aggressively. For instance, ILEC recalcitrance to provide collocation and unbundled xDSL loops – clearly required by Federal law and FCC rules – should be urgently investigated when brought to the FCC's attention, and fines and forfeitures should result if misconduct is found.

3. *Structural Regulation*

Structural regulation attempts to affect positively market performance by establishing "bright line" tests that firms may not cross. Typical examples of structural regulation include ownership limits, standard technological interfaces and standards,[41] and various forms and degrees of structural separation. Like all other forms of regulation, however, structural separation is also not a homogenous regulatory tool. Rather, like all forms of economic regulation, structural separation is question of degree: the stricter the regulatory requirement of "separateness," the higher the cost to the

---

39 *See* Easterbrook, *supra* n. 2, 98 HARV. L. REV. at 40 (1984) (emphasis supplied).

40 *See In re Implementation of the TelecommunicationsAct of 1996, Amendment of Rules Governing Procedures to be Followed when Formal Complaints are filed Against the Commission*, Second Report & Order, ___ FCC Rcd ___, FCC No. 98-154 (rel. July 14, 1998).

41 *See, e.g.*, Part 68 of the FCC's rules, 47 C.F.R. §§ 68.1 et seq., which, by requiring standard technical interfaces, permits competition in the terminal equipment market.

regulated firm. As such, depending on the specific regulatory harm the Commission wants to mitigate or the particular long-term market structure the Commission wants (but has yet to articulate) to achieve, the Commission can avail itself of four primary forms of "structural separation" (each of which is listed in order of most significant economic costs to least imposed economic costs): (1) "line-of-business" restrictions; (2) mandatory separate subsidiaries with outside equity participation; (3) wholly-owned separate subsidiaries; and (4) mandatory separate corporate divisions. As a regulatory alternative to strict structural separation, however, it is also possible to impose strict accounting requirements accompanied by various conduct restrictions or mandates.

Yet, if the Commission routinely fails to undertake the prerequisite cost/benefit analysis necessary to determine – in light of where the FCC wants to see the future market structure to be – what the costs and benefit are of the structural rules the FCC wants to impose, then any FCC initiative will deter rather than accelerate, new infrastructure entry.[42] Unfortunately, promulgating "rules for the sake of rules" is no substitute for reasoned public policy decision-making.

---

[42] Thus, if the FCC really wanted to encourage additional cable overbuilds, it could take such steps as, inter alia: (1) Streamlining and overhauling its OVS Rules to make entry more attractive (indeed, if Internet video is to become a reality, FCC must be *semper vigilans* regarding rivals' attempts to impose access charges on Internet providers); (2) Encouraging new entrants to bundle telephone and video services using Ramsey-pricing methodology (because video is very profitable, such bundling may actually promote additional facilities-based entry for new telephone service); (3) Eliminating DBS exogenous costs (*e.g.*, elimination of restrictions on retransmission of broadcast and network signals by DBS providers); (4) Continuing not to impose "public interest" broadcast requirements on MVPD providers; (5) Waging a battle against local governments using the franchising process and other regulatory forums as a way to extract revenue, obtain "free" coverage of zoning board meetings, and delay entry overall; (6) Ensuring that local fees for digging up the streets should be non-discriminatory; (7) Eliminating must-carry for "qualified low power" stations (*i.e.*, MSOs should be permitted to "chase the eyeballs" – as such, there is no need to continue to subsidize HSN *et al.*); and (8) Eliminating Leased Access and PEG Channel requirements (*i.e.*, the economic rationale for eliminating these programs is the same for the elimination of PTAR in broadcasting and for the elimination of must-carry for low-powered stations).

For example, one of the most significant barriers to entry for new infrastructure development are regulatory and legislative "buildout" requirements" – *i.e.,* requirements that a new entrant must serve *all* of the franchise territory before it can begin providing service, rather than using an entry strategy that initially targets select areas.[43] This barrier is simply exacerbated when the buildout requirements also require new entrants to build capacity in excess of their own needs for the benefit of potential competitors (*see, e.g.,* OVS buildout requirements). Indeed, considering the considerable sums new entrants must sink (and accordingly risk) to enter an already concentrated market, any requirement that a new entrant must also build additional capacity *for its competitors* well in excess of its own needs simply makes entry unattractive. Moreover, these requirements seem to contradict regulations imposed on the telephone side, where the Commission attempts to spur immediate competition through resale and UNEs, thus

---

[43] *See, e.g.*, Cable Act Section 621(a)(3), and by implication, Cable Act Section 621(a), which provide in pertinent part that:

> (3) In awarding a franchise or franchises, a franchising authority shall assure that access to cable service is not denied to any group of potential residential cable subscribers because of the income of the residents of the local area in which the group resides.
>
> (4) In awarding a franchise, the franchising authority ---
>
> > (A) shall allow the applicant's cable system a reasonable period of time to become capable of providing cable service to all households in the franchise area.

Thus, for example, under current rules, if a SMATV strings a line over a public right of way, it becomes a cable operator and therefore subject to cable rules and obligations -- including buildout requirements. Yet, one of the quickest services of cable competition in many areas would be from SMATVs serving adjacent buildings and neighborhoods, because there are few alternative firms that already possess the sufficient economies of scale and scope (e.g., perhaps a LEC or maybe a public utility) necessary to pass existing buildout requirements (i.e., the new entrant must serve an entire franchise area before having a single customer) to make immediate entry likely.

permitting new firms to enter in limited areas without having to complete a full overbuild of the incumbent's network.

IV. Specific Critiques

As stated above, TEC has absolutely no desire to rehash the numerous specific issues that have already been litigated *ad nauseam* before the Commission. Rather, as instructed by the plain language of Section 706 of the 1996 Act, this inquiry seeks to take a broader view of the issue. In the spirit of this inquiry, TEC will focus on what it believes are two of the most critical policy approaches where the FCC's actions (or lack thereof) have unintentionally deterred, rather than promoted, new advanced infrastructure development and deployment – *i.e.*, (1) the FCC's current universal service program; and (2) the FCC's failure to use aggressively its "bully pulpit" or either its 253 and Section 10 authority to forbear or pre-empt laws and regulations that dramatically deter new advanced infrastructure deployment. Each are set forth below.

A. *How Current Universal Service Policies Act as a Significant Barrier to Entry (and thus a Self-Defeating Exercise)*

As a general proposition, universal service is certainly a worthy social goal and a very important public policy. Tragically, the greatest impediment to true universal service (*i.e.*, the notion that "all the people of the United States, without discrimination on the basis of race, color, religion, national origin, or sex," should have, "so far as possible" access to a "rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges"[44]) has been the FCC's own policies – not any action by the market – that act as substantial barriers to entry and dead weight loss to society.[45]

Once again, regulation and competition are supposed to be substitutes, not complements. Similarly, the whole purpose of the 1996 Act was ostensibly to promote competition and lead to deregulation.[46] It seems a bit paradoxical, therefore, that Congress rationally believed that society could have *both* "competitive" markets yet, at the same time, require firms (a) to guarantee that everyone will receive reliable service, and moreover (b) to ensure that particular sectors of society will enjoy not only "reliable" service but also some sort of *subsidized* service as well.[47]

---

44 See Communications Act Section 1, 47 U.S.C. § 151.

45 *See* Jerry Hausman, *Taxation by Telecommunications Regulation, in* Tax Policy and the Economy (forthcoming 1998) (calculating that the efficiency loss to society of policy to raise $2.25 billion per year to fund an Internet subsidy to schools and libraries to be approximately $1.25 per dollar raised, or a total of approximately $2.36 billion per year (in addition to the $2.25 billion per year of tax revenue)); Robert J. Samuelson, *Telephone Straddle*, Wash. Post, May 14, 1997, at A21.

46 *See* Janet Reno et al. v. American Civil Liberties Union, 117 S. Ct. 2329, 2337-38 (1997) (Telecommunications Act of 1996 was "an unusually important legislative enactment" because its "primary purpose was to reduce regulation and . . . to promote competition in the local telephone service market, the multichannel video market, and the market for over-the-air broadcasting").

47 *See* Thomas G. Krattenmaker, *The Telecommunications Act of 1996*, 49 FED. COMM. L.J. 1, 41-43 (1996) ("[u]niversal service, as defined in the new Act, and competitive markets cannot coexist, where the goods produced have many substitutes or where the technology is dynamic." Accordingly, argues Krattenmaker, "*it is both bad competition policy and bad regulatory policy to think that one can achieve properly functioning telecommunications markets while a regulator sees to it that these same markets generate subsidized pro-societal benefits.*")(Emphasis supplied.); *What Hath Congress Wrought? Reorienting Economic Analysis After the 1996 Act,* ANTITRUST (American Bar Assoc. Spring 1997) 32, 34 and citations therein; *see also* Harold Demsetz, *Barriers to Entry,* 72 AM. ECON. REV. 37-47 (1982); William J. Baumol *et al.*, CONTESTABLE MARKETS AND THE THEORY OF INDUSTRY STRUCTURE 362 (1988); Easterbrook, *supra* note 2, at 15-16 ("[P]eople demand laws just as they demand automobiles, and some people demand more effectively than others. Laws that benefit the people in common are hard to enact because no one can obtain very much of the benefit of lobbying for or preserving such laws." As such, because "cohesive groups can get more for themselves by restricting competition and appropriating rents than by seeking rules that enhance the welfare of all . . . we should expect regulatory programs and other

Yet, as if implementing Congress's apparent schizophrenic policy objectives wasn't difficult enough, the FCC inadvertently made matters far worse by deliberately politicizing the universal service program to advance improperly the Administration's schools and libraries program. In fact, the FCC actually hindered and delayed new advanced telecommunications services to schools, libraries, hospitals and rural areas, because not only does a mandatory universal service requirement – and, in particular, the mandatory requirement that *all* "providers of interstate telecommunications" that offer such telecommunications "to others for a fee" must contribute substantial sums of their *gross* revenues to the universal service fund[48] – impose a significant dead weight efficiency loss on consumer welfare,[49] but, in more practical terms, such a policy also acts as a *major* barrier to entry for new firms. This regulatory barrier to entry is simply exacerbated by the fact that, with one exception discussed *infra*, neither the FCC nor the courts have yet to apply these definitions to any individual cases, hence it is unclear who or what will ultimately be called on to contribute to the fund and how much they will owe. Thus, not only would "typical" providers of interstate telecommunications be required to contribute to the fund (*e.g.*, common carriers and private line operators of

---

statutes to benefit the regulated group. . . ." Accordingly, these groups "*need not 'capture' the programs, because they owned them all along. The burgeoning evidence showing that regulatory programs increase prices for consumers and profits for producers supports this understanding.*" (emphasis supplied and citations omitted)); *see also* George Stigler, *The Theory of Economic Regulation*, 2 BELL J. ECON. & MGMT. SCI. 2-21 (1971). The Commission should also be aware that its current universal service program is great consternation abroad as well. *See* David Molony, *EC and U.S. to Clash Over Universal Service Funds*, COMMUNICATIONS WEEK INTERNATIONAL (April 6, 1998).

[48] *See Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report & Order, FCC 97-157 (rel. May 8, 1997) at ¶¶ 794-96.

[49] *See* Hausman, *supra* note 45.

telephone or wireless companies) but, more importantly, firms that just *incidentally* may be in telecommunications could be required to contribute. These types of firms could range anywhere from a utility that simply seeks to lease dark fiber to a CLEC, to a Seven-Eleven convenience store that sells phone cards. In addition, because the universal payments are characterized, as of the time of this writing, as "contributions," these "contributions" may not be deducted on a contributing firm's tax return. [50] Accordingly, if a new entrant (or even an existing firm) perceives that the costs imposed by the 1996 Act's mandatory universal service obligations and payments may actually exceed[51] the initial profits it hopes to receive, then entry (or a continued presence in the market) will not be economical and will not occur.[52]

Even more appalling is that entrants do not know how much they will owe to the fund until "bills" are sent out. The FCC revises the USF contribution factors every six months, and those factors are calculated to cover expected costs. Providers are then required to pay that percentage of their revenue from the *prior year*. The result is that a

---

[50] What is particularly disturbing about this scenario is the fact that this exact type of non-price competition is one of the major reasons why it is highly unlikely that long-distance carriers can successfully engage in some sort of tacit collusion under current market conditions. *See Reorienting Economic Analysis, supra* note 47, at 35.

[51] Perhaps if Congress is really so concerned about wiring the schools, a direct tax *credit* may be a better way to go – *i.e.*, we eliminate the "middle man" and carriers can get direct positive public-relations benefits from the whole endeavor. This approach might even *encourage* entry! As the empirical evidence unfortunately shows, a multi-billion dollar fund creates just too many incentives for nefarious behavior. *See, e.g.*, James K. Glassman, *Gore's Internet Fiasco*, WASHINGTON POST (June 2, 1998) at A13.

[52] *See* Scott Cleland, *Subsidy Reform – Big Skunk at the Competition Picnic?* Telecom Watch (Wash. Research Group, Apr. 25, 1997) ("FCC's subsidy reform of universal service and access charges will prove to be a larger *impediment* to the development of local competition than most appreciate."); Samuelson, *supra* note 45 (while Universal Service's "educational benefits may be phantom . . . the higher overall phone rates needed to pay for them aren't"; moreover, while the "subsidies for the poor may be justified[, t]he rural subsidy isn't. *If people prefer to live in rural Montana, they should enjoy the pleasures and bear the costs.*" (emphasis supplied)).

provider can only guess how much of the revenues it generates today will be taxed next year, because today no one can accurately estimate what next year's USF expenses will be. Imagine that you are a telecommunications provider and you are attempting to put together your balance sheet (particular, your accrued liabilities account) for an SEC filing – how do you explain to your auditor your justification for reserving 2%, 4% or even 6% of your gross interstate telecommunications revenues for possible taxation next year? This retroactive taxation is unconscionable, and the resulting uncertainty serves only to decrease the changes that a firm will enter the telecommunications industry, as opposed to other industries where changes in tax rates only apply prospectively.

More importantly, however, is that the Commission apparently believes erroneously that all entrepreneurial firms have some sort of "captured" ratebase just like an established firm, such that they can ensure a constant stream of contributions to the USF. The problem, however, is that entrepreneurial firms, by definition, do not have a steady or guaranteed revenue stream. It is therefore wholly inappropriate for the Commission to talk about taxing gross revenues when entrepreneurial firms are attempting to assuage their venture capital investors by producing positive net revenues – an exercise which is essential to continued survival in the first instance. The FCC further exacerbates this already difficult entrepreneurial challenge by imposing additional universal service charges that actually force entrepreneurs' prices to rise – and, *a fortiori*, become less attractive and competitive to established firms' products and services – than they would otherwise be.

The one instance where the Commission did provide some clarity was in its recent report to Congress on Universal Service (*a.k.a.* the "Stevens Report").[53] In the Stevens Report, the Commission decided that it would consider imposing access charge and universal service contributions (albeit on a case-by-case basis) on Internet telephony (IP) providers, which, if adopted in practice, would eviscerate nearly fifteen years of past precedent.[54] At the time of the original *Computer II* inquiry, more enlightened forward-looking FCC staff realized that technological developments may reach a point where enhanced services may truly be a close substitute for traditional, switched-voice services. Rather than attempting to regulate these developments, the FCC decided to let this process begin. Yet – low and behold – just when technology finally has caught-up and IP telephony (complete with the concurrent construction of new state-of-the art networks) is now starting to exert desired downward pressure (both domestically and especially internationally) on the need for universal service and access charges, the FCC has set the stage to pull a regulatory "bait and switch." Specifically, the Commission is now improperly attempting to claim that it is *reducing* the amount each industry participant may contribute overall *yet, at the same time, the Commission is actually increasing the number of people who must contribute to the fund!* Accordingly, the Commission has done nothing more than surreptitiously ensure that the overall amount in the universal service fund arguably will stay the same by deterring competition and denying consumers

---

[53] *In re Federal-State Joint Board on Universal Service*, Report to Congress, ___ FCC Rcd ___, FCC 98-67 (re;. April 10, 1998).

[54] *Id.* at ¶¶ 83-93.

access to the additional choices and lower prices they deserve and expect.[55] Thus, no one should really be surprised when incumbents immediately attempted to do what the FCC stated that they now were apparently entitled to do (*i.e.*, impose access charges on IP providers).[56]

B. *To Regulate or Not to Regulate: Forbearance, Pre-emption and the Bully Pulpit.*

1. *Forbearance*

TEC recognizes the Commission is in the midst of an agency-wide biennial review of its regulations pursuant to Section 11 of the Communications Act, as amended by the Telecommunications Act of 1996.[57] TEC hopes that as the Commission undertakes this process, however, it does so in a truly meaningful fashion. Indeed, while the elimination of such obviously ridiculous and outdated rules, for example, to protect spectrum for "those persons regularly engaged in . . . [t]he delivery of ice . . . to the consumer for refrigeration" (47 C.F.R. § 90.7) is laudable, the true challenge before the FCC is not so benign. Accordingly, the Commission's recent practice of talking the "de-regulation" rhetoric in the beginning of a Commission item while all the while actually imposing *more* regulation at the end of the item by having firms comply with a myriad of

---

55 As a side note, TEC's members strenuously object to the plethora of *ad homonym* attacks leveled against anyone who opposes the current universal service system. It is incumbent for everyone in the process to discuss constructively the various differences about the way to best provide service to schools, hospitals and rural areas.

56 *See Official Says FCC Hasn't Ruled on IP Telephony Access Charges*, TRDAILY (Sept. 8, 1998).

57 47 U.S.C. § 161.

burdensome and/or obtuse (not to mention often analytically and legally inconsistent) requirements or, more egregiously, accepting "voluntary" conditions, simply has to stop.

2. *Pre-Emption*

One of the other major impediments to entry is the local and state regulatory/legislative process. The FCC has had several opportunities to pre-empt these laws – and thereby promote competition – but unfortunately has squandered some of the opportunities with which its has been presented.

For example, when it came time for the FCC to pre-empt state laws that prevented rural municipal utilities and cooperatives (*i.e.,* entities that actually have an existing network in place) from immediately providing competitive telecommunications service to those exact areas where universal service is needed the most, the FCC refused to pre-empt a state law that significantly impedes this very process. In doing so, the Commission has now tragically condoned implicitly *all* such laws.[58]

As support for this decision, the FCC argued that it lacked the jurisdiction to pre-empt this law because these municipal utilities were "creatures of the state" and, as such, the state can tell them exactly what they may and may not do. Of course, last time we checked, all corporations are "creatures of the state" and derive their powers to act through state-approved articles of incorporation. Moreover, if everyone is supposedly so

---

[58] *See In re Public Utilities Commission of Texas, et al.,* Memorandum Opinion and Order, ___ FCC Rcd ___, FCC No. 97-346 (rel. Oct. 1, 1997).

serious about promoting competition, it seems a bit hypocritical that states are often more than willing to protect municipals' exclusive monopoly franchise status for electricity, but are wholly reluctant to permit these municipal utilities to enter into telecommunications and provide head-to-head, facilities-based competition against the incumbent LEC.[59]

Recent reports indicate that there are about 2,000 utilities owned by governments and that there are about 910 rural electric cooperatives. Collectively, they own assets that exceed $20 billion dollars.[60] More importantly, however, given the existing service areas of many municipal utilities and especially rural coops, these utilities are well posed to provide telecommunications service to those high-cost areas where incumbent carriers are reluctant to go – even with universal service support payments. Indeed, the whole reason municipals and coops were created originally was because private, profit-making companies bypassed smaller towns to go after more profitable markets.[61] Accordingly, if universal service is truly a "worthy social goal," then TEC would far rather have a local municipal utility or coop fill the void – and provide necessary community services and be a powerful engine for local economic growth – than perpetuate the Commission's

---

[59] Attempts at deterring municipal utility entry arise in basically two ways: First, a municipal utility's original corporate charter failed to include language that it can also provide telecommunications services and products. Thus, the minute the muni goes to the state legislature to have its charter amended, the process magically becomes bogged down in committee. The second scenario is more disturbing. All around the country, numerous states such as Texas, Missouri, Nevada, Nebraska, Florida, Georgia and Arkansas are currently deliberating, or have already passed, laws which outright prohibit municipal utility into telecommunications yet, at the same time, subject them to universal service obligations.

[60] *See* Geof Petch, *Here Comes Ready Kilowatt,* X-CHANGE MAGAZINE (May/June 1996) at 34-35.

[61] *See* Geof Petch, *How a Small Town Became a Digital Veg-O-Matic (and Accidentally Reinvented the Concept of Public Utility),* X-CHANGE MAGAZINE (Sept. 1996) at 46.

existing distorting and expensive universal system of embedded incentive-reducing subsidies.[62]

3. *The "Bully-Pulpit"*

Even where the FCC lacks the legal authority to waive, forbear or pre-empt, the FCC has been unfortunately reticent about using its "bully-pulpit" to advance a pro-competitive agenda, particularly when it comes time to criticize legislative or political initiatives that deter new infrastructure development and competition. Accordingly, so long as the FCC holds itself out before the courts and the public as the independent agency with significant expertise about telecommunications issues, the Commission is going to have to start to lead by example. As discussed supra, even though a *tabla rasa* approach is not a political or legal possibility at this time, the FCC can contribute positively to the process by showing specifically why, where, when and how particular policy proposals will succeed or fail and, moreover, providing a well reasoned alternative

---

[62] Indeed, the Glasgow, Ky. Municipal Utility Plant Board's broadband system keeps more local cash at home by producing over $1.2 million per year in reduced cable rates and $175,000 in savings through more efficient distribution of power. *Id.*

As an additional note, the NOI also asks whether utilities in general (especially investor-owned utilities) have an incentive to begin providing advanced services on a wide scale. NOI at ¶¶ 47-49. The sad reality is that while utilities are among the most promising new entrants for additional infrastructure (and in fact, several utilities such as Central & SouthWest, Connectiv, and Southern Co. have made significant inroads in this area), there are several factors that are deterring generic utility entry for new infrastructure in any meaningful way. On one hand, because utilities are too busy trying to survive FERC's economically and legally flawed restructuring paradigm, they have little incentive to enter ancillary telecommunications markets. Obviously, these factors are beyond the Commission's authority but it should be made aware of it nonetheless. *See Utility Entry into Telecommunications: Exactly How Serious Are We?* PHOENIX CENTER PUBLIC POLICY PAPER SERIES NO. 1 (1998) (http://www.phoenix-center.org/pcpp/pcpp1.doc), *Three Reasons Why Utilities Need Telecommunications Expertise – Whether They Like it or Not,* INFRASTRUCTURE (American Bar Association Spring 1998). On the other hand, however, the various critiques of the Commission's purported pro-entry policies discussed *passim* affect utilities – just like any other entrant. Accordingly, the Commission does play a role after all.

proposal to further the debate, for example, by acting to the extent its legal authority with respect to building access. At the same time, moreover, the Commission must aggressively coordinate with state authorities as to the legislative and/or other policy relief necessary not only to fully ensure that consumers have the ability to select freely a service provider of their own choice (ultimately dial-tone and advanced telecommunications services), *but that carriers can provide these products and services to end-users over the distribution network of their choice as well.* Timid procrastination or asking for public comment *ad nauseum* without ever reaching a definitive decision simply will not suffice any more.

V. Conclusion

In conclusion, TEC reminds the Commission that it cannot stretch the word "public" in public utilities to such an absurd point that it forgets that telecommunications and related industries is a high-stakes business as well. So long as the Commission improperly attempts to promote "neo-competition," as opposed to true tangible entry and infrastructure investment, then this so-called "transition" period may be a very long and dark time for consumers to endure.

Respectfully submitted,

Lawrence J. Spiwak
General Counsel
Technology Entrepreneurs Coalition
5335 Wisconsin Avenue, NW
Suite 440
Washington, D.C. 20015
www.tec-coalition.org

September 14, 1998